

CalPERS' Actuarial and Retirement Benefits Seminar

■ **Rate Volatility**

■ **Rate Stabilization**

■ **Preview 2006-07 Rates**

■ **Pooling**

■ **GASB 45**

Pooling

- Pooling was **Implemented** for the June 30, 2003 Valuation for the **2005-06** Fiscal Year
- To **Stabilize** Contribution Rate Volatility in **Small Plans**
- Caused by **Demographic Experience**
- “Law of Large Numbers” Doesn’t Apply in Small Plans

Best Understood by an Example

- Hypothetical Assumption is that 1 In 100 Members will Retire Under Industrial Disability in the Coming Year
- 1 Member in 1st Rate Plan Retires Under IDR, We Expected 1/10 of a Member and Got 1 Member; No IDR in Plans 2-9, We Expected 1/10 and Got 0 Each, So Small Gain

plan #	active members	payroll	assets	expected accrued liability	actual accrued liability	(gain) loss	1/16 amt pmt	% of pay change in rate
------(in thousands)-----								
1	10	500	5,000	4,000	4,360	360	22.5	4.5%
2	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
3	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
4	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
5	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
6	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
7	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
8	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
9	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
10	10	500	5,000	4,000	3,960	(40)	(2.5)	-0.5%
pool total	100	5,000	50,000	40,000	40,000	-	-	0.0%

- Pooling will Ultimately **Simplify** the Actuarial Process
- **Sharing** of Liability (or Demographic) Gain and Loss **Begins June 30, 2003**

Pool Data from June 30, 2003

pool	misc safety	formula	plans	net normal cost	asset to payroll ratio
1	misc	2%at60	277	6.46%	2.2
2	misc	2%at55	537	7.58%	2.7
3	misc	2.5%at 55	45	8.37%	3.2
4	misc	2.7%at55	76	9.25%	3.1
5	misc	3%at60	52	10.53%	3.0
6	safety	2%at55	64	11.16%	2.5
7	safety	2%at50	129	11.51%	4.9
8	safety	3%at55	78	13.06%	5.6
9	safety	3%at50	175	15.33%	6.2

Leveling the Playing Field

At June 30, 2003 Implementation

- Problem - Different **Funding Levels**
- ✓ Solution - Separate Side Funds Equal to Unfunded at June 30, 2003 are the Responsibility of Rate Plan – Not Shared
- Problem - Different **Optional Benefits**
- ✓ Solution – Surcharge for “Class 1” Optional Benefits, Adjust Side Fund for “Class 2”, No Charge for “Class 3”

Class 1, 2 and 3 Benefits are Described in Each “Pool Valuation Report”

- **Following is an Excerpt from Appendix C of the 2% at 55 Risk Pool Valuation as of June 30, 2003**

CLASS 1

Class 1 benefits have been identified to be the more expensive ancillary benefits. These benefits vary by employer across the risk pool. Agencies contracting for a Class 1 benefit will be responsible for the past service liability associated with such benefit and will be required to pay a surcharge established by the actuary to cover the ongoing cost (normal cost) of the Class 1 benefit.

The table below shows the list of Class 1 benefits and their applicable surcharge for the Miscellaneous 2% at 55 Risk Pool.

Class 1 Benefits	Applicable Surcharge
One-Year Final Compensation	0.501%
Employer Paid 7% Member Contributions Converted to Payrate During the Final Compensation Period	0.899%
Employer Paid 8% Member Contributions Converted to Payrate During the Final Compensation Period	N/A
Employer Paid 9% Member Contributions Converted to Payrate During the Final Compensation Period	N/A
25% Post-Retirement Survivor Allowance	0.861%
50% Post-Retirement Survivor Allowance	0.861%
3% Annual Cost-of-Living Allowance Increase	1.148%
4% Annual Cost-of-Living Allowance Increase	1.148%
5% Annual Cost-of-Living Allowance Increase	1.148%
Industrial Disability Retirement for Local Miscellaneous Members	0.523%
Increased Industrial Disability Allowance to 75% of Final Compensation	0.931%
Improved Industrial Disability Allowance for Local Safety Members	N/A
1.00% Employees Sharing Cost of Additional Benefits	(1.000%)

CLASS 2

Class 2 benefits have been identified to be the ancillary benefits providing one-time increases in benefits. These benefits vary by employer across the risk pool. Agencies contracting for a Class 2 benefit will be responsible for the past service liability associated with such benefit.

The following benefits shall be classified as Class 2:

- One-time 1% to 6% *Ad Hoc* COLA Increases for members who retired or died prior to January 1, 1998 (Section 21328)
- "Golden Handshakes" – Section 20903 Two Years Additional Service Credit
- Credit for Prior Service Paid for by the Employer
- Military Service Credit (Section 20996)
- Credit for Local Retirement System Service for Employees of Agencies Contracted on a Prospective basis (Section 20530.1)
- Prior Service Credit for Employees of an Assumed Agency Function (Section 20936)
- Limit Prior Service to Members Employed on Contract Date (Section 20938)

CLASS 3

Class 3 benefits have been identified to be the less expensive ancillary benefits. Class 3 benefits may vary by rate plan within each risk pool. However, the employer contribution rate will not vary within the risk pool due to the Class 3 benefits.

The following benefits shall be classified as Class 3:

- Full formula plus social security (Section 20515)
- Post Retirement Lump Sum Death Benefit
- \$600 lump sum retired death benefit (Section 21622)
- \$2,000 lump sum retired death benefit (Section 21623.5)
- \$3,000 lump sum retired death benefit (Section 21623.5)
- \$4,000 lump sum retired death benefit (Section 21623.5)
- \$5,000 lump sum retired death benefit (Section 21623.5)
- Improved non-industrial disability allowance (Section 21427)
- Special death benefit for local miscellaneous members (Section 21540.5)
- Service Credit Purchased by Member
- Public Service for Peace Corps or America Corps: VISTA Service (Section 21023.5)
- Public Service Credit for Employees of an Assumed Agency or Function (Section 21025)
- Public Service Credit for Limited Prior Service (Section 21031)
- Partial Service Retirement (Section 21118)
- Optional Membership for Part Time Employees (Section 20325)
- Extension of Reciprocity Rights for Elective Officers (Section 20356)
- Removal of Contract Exclusions Prospectively Only (Section 20503)

Mandatory Benefits

- **Credit for Unused Sick Leave**
- **Option 2 Pre-retirement Death Benefit**

Sharing Of Normal Cost

- On a Stand Alone Basis, the Normal Cost % Will Vary Among Plans with the Same Benefits
- Normal Cost % Depends on **Average Entry Age** for Active Members
- Older Entry Age = Higher Normal Cost %
- Pooling “Phases Out” these Differences Over 5 Years

Normal Cost Phase-out (Example)

Pool "net" normal cost	6.5%	Normal cost	
Class 1 surcharges		<u>Year</u>	
FAC 1	0.5%	2005-06	8.2%
<u>PRSA</u>	<u>0.7%</u>	2006-07	8.1%
Pool normal cost	7.7%	2007-08	8.0%
<u>Agency normal cost</u>	<u>8.2%</u>	2008-09	7.9%
Difference	0.5%	2009-10	7.8%
Annual phase out (5-yr)	0.1%	2010-11	7.7%

Contribution Rate Components

- **Non-Pooled Plan Contribution Rate Consists of Two Components**
 - Normal Cost +
 - Amortization of Unfunded
- **Pooled Plan Contribution Rate has Five Components**

Hypothetical Example of Five Components of Pooled Plan Cost For 2006-07

Year	2006-07
Pool's "net" normal cost	6.5%
Pool's payment on amortization bases	0.5%
Class 1 surcharges	1.2%
Phase out of normal cost difference	0.4%
<u>Amortization of side fund</u>	<u>5.0%</u>
Total employer contribution	13.6%

Amendments

- **For Optional Benefit, Apply New Surcharge and Increase Side Fund for Change in Accrued Liability**
- **For New Formula, Move to New Pool with New Normal Cost and Surcharges, Adjust Side Fund, Same Normal Cost Phase Out**

Voluntary Pooling - Agencies

- **Subject to Approval by Chief Actuary**
- **Potentially Smoother Costs than Single Non-Pooled Plan**

Voluntary Pooling - Schools

- **Improve Benefits to “AB616” Formula**
- **2.5% at 55 May Not Be Available**
- **May Not Apply to Past Service**
- **Legal Remedies Being Sought**

Additional Contributions

- Side Funds – OK to **Pay Off** Side Fund with Single Lump Sum Contribution (e.g. POB)
- However, **Cannot Create a Surplus** Side Fund Through Additional Contributions
- Such Additional Contributions Will Be Held in **2nd Side Fund** and Credited with **Actual Fund Earnings**

Other Issues

- Differences in IDR Experience
- Payroll Increase Gain(Loss)
- Contribution Gain(Loss) and Prepayments
- Vouchers
- New Agencies and the Pool's Amortization Payment

End Pooling Section